

THE LEASING QUESTION

Leasing became popular when businesses wanted to operate automobile fleets while avoiding the high cost of ownership and maintenance. When individual leasing developed, consumers were faced with a new market question: to lease or not to lease.

Automobile leasing is not a simple matter. Cars lose value or depreciate over time. When you lease a car for two years, you are paying for two years of depreciation in monthly payments plus interest. At the end of the lease, the automobile can be either sold to you or someone else for its value at that point. There is no ownership, you simply pay for the use of the automobile. The manufacturer's warranty covers most repairs but all maintenance costs and insurance are your responsibility.

The new Regulation M from the Federal Reserve Board, effective January 1, 1998, requires disclosure by leasing companies of specific information and provides consumers with a description in writing of the lease's financial details. A model disclosure form is available. The stated purpose of the new Regulation M is to allow consumers to compare one lease with another for the same vehicle and to compare leasing a vehicle with buying it on credit. However, the disclosure requirements do not apply to lease transactions over \$25,000.

LEASING TERMS

Lessee. The consumer.

Lessor. The company that owns the automobile.

Gross capitalized cost. The price of the car for leasing purposes.

Capitalized cost reduction. Amount of cash down payment, trade-in or rebate.

Residual Value. The automobile's value at the end of the lease. Also known as guaranteed future value or lease-end value. It is often expressed as a percentage of the Manufacturers Suggested Retail Price (MSRP). The higher the residual value, the less depreciation you pay. The residual value may be a negotiable figure. To determine it, many dealers consult a publication called Automotive Leasing Guide, a useful tool for predicting future value.

Payment Amount. An amount paid by the lessee that may include interest, overhead and profit.

Money Factor. This figure, also known as the lease rate or monthly lease fee, is the interest rate built into all leases. It is leasing's version of the annual percentage rate of interest (APR) that is charged to people who buy on credit. Leasing companies do not usually disclose the money factor except when competing with other lessors.

ADVANTAGES TO LEASING

The monthly payment is lower than when buying a car. In some cases there is no down payment at all.

Leasing puts the driver in a new car every two or three years. For some consumers, this is an important lifestyle consideration. Leasing also allows consumers to drive a more expensive vehicle than they can afford to buy.

Leasing is easier since negotiating over the price is downplayed.

Vehicles are subject to wear as they age. A lease allows consumers to side-step the issue. By the time the car needs expensive repairs, the lease will have ended.

There is no hassle with a trade-in at the end of the lease.

Current tax law considers many of the expenses of a lease car used for business to be tax deductible.

DISADVANTAGES OF LEASING

When the lease ends, you have built up no equity in a vehicle. You have nothing to trade in on a new car, so you will probably lease again.

If a lease runs longer than the vehicle's warranty, the lessee may have to pay for repairs that would have been covered.

In most cases, leasing is more expensive than buying on credit.

Maintenance requirements for leased vehicles are strict if the lessee hopes to avoid end-of-lease charges. A lessee should honor the manufacturer's recommended maintenance schedules and should have written receipts to prove that service was performed as required.

Early termination of a lease may result in substantial charges to the lessee.

STEPS IN AUTOMOBILE LEASING

Know the important questions to ask before you lease a car. There are major differences between buying and leasing. However, the first steps in leasing are the same as those in buying a car.

Collect information. Select the model you are interested in and record the identifying data at the dealership. Negotiate a fair price for the car and get a price commitment on your trade-in. Ask the salesperson to have the agreement written up as a lease.

Negotiate the gross capitalized cost. Try to negotiate a gross capitalized cost somewhere between the MSRP and the dealer invoice price. The lower the cap cost, the better deal for the consumer. If the gross capitalized cost is too high, tell the salesperson to cut items that increase the total cost. If the salesperson claims that capitalized cost is a fixed figure and can't be lowered, find another salesperson. Use the required disclosure form as a worksheet. On the form, compare the agreed upon value of the vehicle with the gross capitalized cost to see what charges have been added.

The law of supply and demand affects leasing as well as buying. If car sales are breaking records and the model you want to lease is a hot seller, expect to pay more. If the opposite is true and car sales are sluggish, bargain for a capitalized cost that represents a discount from the MSRP.

Filled in disclosure form. Ask the salesperson to fill in the disclosure form front and back and give you the figures. Be sure that you check the box near the middle of the front page in order to get a step-by-step calculation of the monthly payment. At this time, lessors are not required to provide data on the money factor used to calculate the equivalent of the annual percentage rate of interest (APR) charged on vehicle loans.

Review the disclosure form. Ask for explanations of any items you do not understand. Make sure that the trade-in allowance reduces the gross capitalized cost. In the past, a common leasing complaint was that consumers were not given credit for the trade-in. To prevent this, scrutinize the line on the disclosure form titled capitalized cost reduction. The total amount should include rebates, cash down payment, and trade-in allowance. If you have paid a deposit, make sure you get credit for it.

Take the lease home and study it. Once the lease is written, instead of signing on the spot, ask for an exact photocopy to take home and study. Given the importance of the document, the obscurity of its terms, and its legally binding status, a quick decision is not smart. If possible, avoid giving a deposit at this stage since there is no deal until you sign the lease.

Compare the figures. At home, compare the figures on the lease with those on your disclosure form. Look for unexplained changes. Use your calculator to check the math. Verify the accuracy of the most important figures: lease term, gross capitalized cost, capitalized cost reduction, residual value, and rent charge.

A short-term lease, up to 24 months, means larger payments and more money spent for depreciation. A longer lease, up to 48 months, should have smaller payments, but may be less flexible. Experts recommend a lease length that coincides with the length of the vehicle's warranty.

END-OF-LEASE COSTS AND OTHER CONSIDERATIONS

When you buy an automobile, the hard bargaining and stressful confrontations often come at the beginning of the deal. In contrast, leasing is quite simple at the onset but potentially complicated at the end. When you turn the car in, problems may develop. They can be avoided by reading the fine print, sentence by sentence, before you sign. Some of the important items to look for are:

Gap Insurance. If the lease car is totaled or stolen, your auto insurance may cover replacement but not the payments still required. Gap insurance covers the difference between the replacement value of the car and what is still owed on the lease. It is expensive to purchase separately. Ask if it is included without charge to the lessee.

Excess Wear and Tear. At the end of the lease, if the car has visible damage, the consumer will probably be charged to repair it. To protect yourself, get a copy of the written guidelines or checklist issued by leasing companies. Of course, the longer the lease, the more likelihood of an excess wear charge. Some leasing companies have made the marketing decision to downplay minor dings, scratches, and upholstery stains. If no damages are assessed, the security deposit will be mailed to you shortly after the automobile is returned.

Excess Mileage. The yearly mileage limit should exceed your normal driving needs. If it does not, find out the charge for additional miles. Try to negotiate a more favorable rate for added miles at the outset.

Disposition Fees. This end-of-lease charge covers costs for picking up and processing the returned car for sale. Some leasing companies do not charge a disposition fee or an acquisition fee, but instead include the costs in the monthly payment. Also, some dealers will absorb the fee if the customer is planning to sign another lease.

Purchase Option. Many leases include the chance to buy the automobile at the end of the lease. The disclosure sheet should tell you if the purchase price is pre-determined or negotiated at the end of the contract. In cases where the residual value has been boosted to a very high level, do not pay more than market price for a car. When examining the contract, see if there is a purchase option fee.

Early Termination and Default. You may incur significant penalties if you break the lease. For example, you may be required to pay 100% of all the remaining payments. A detailed explanation of early termination fees is required by the disclosure form. Although some

leases can be broken with less penalty than others, early terminations are a big cause of disputes.



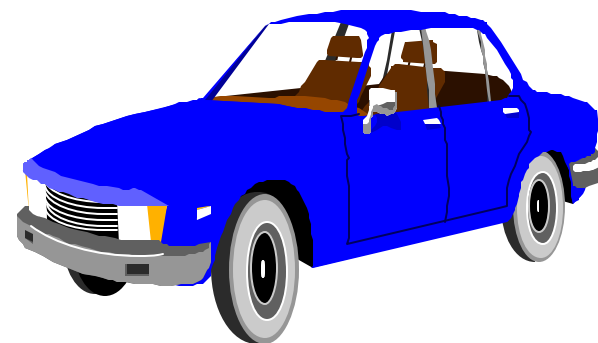
The Indiana Department of Financial Institutions, Division of Consumer Credit has many other credit related brochures available, such as:

Answers to Credit Problems
Applying for Credit
At Home Shopping Rights
Bankruptcy Facts
Buried in Debt
Car Financing Scams
Charge Card Fraud
Choosing A Credit Card
Co-Signing
Credit and Divorce
Credit and Older Consumers
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Call our toll-free number or write to the address on the cover for a copy of any of the brochures listed or for further consumer credit information.



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